Accounting Standard Board, Nepal

Decision on Carve-outs in NFRS with Alternative Treatments

The 143rd Meeting of the Accounting Standard Board, Nepal held on July 15, 2022 (2079 Ashad 31) resolved the following Carve-outs in NFRS with the following Alternative Treatment and effective Period of Carve-outs.

Nepal Rastra Bank has submitted a formal request to the Accounting Standard Board, Nepal on Ashad 30, 2079 for carve-outs on NFRS 9 (Effective Interest Rate), NFRS 9 (Impairment) based on the submission of the Nepal Bankers Association on behalf of the Banks & Financial Institutions of Nepal.

The Accounting Standards Board, Nepal reviewed the request of Nepal Rastra Bank including the justifications provided in detail and has considered the following carve-outs/deferrals in NFRS 9 (Effective Interest Rate and Impairment) for the Banks and Financial Institutions. The other entities may also use these carve-outs with necessary disclosures.

NFRS Reference Number	Existing provision	Carve-out: Alternative treatment	Carve-out/Deferral period
NFRS 9: Financial Instruments			
Para 5.4 read together with appendix A (Defined Terms) relating to *Effective Interest Rate*	*Effective interest rate* is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the **gross carrying amount of a financial asset** or to **the amortised cost of a financial liability.** When calculating the effective interest rate, an entity shall estimate the expected cash flows by considering all the contractual terms of the financial instrument (for example, prepayment, extension, call, and similar options) but shall not consider the **expected credit losses**. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate (see paragraphs B5.4.1–B5.4.3), **transaction costs**, and all other premiums or discounts. There is a presumption that the cash flows and the expected life of a group of similar financial instruments can be estimated reliably. However, in those rare cases when it is not possible to reliably estimate the cash flows or the expected life of a financial instrument (or group of	***Effective interest rate*** is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset or to the amortised cost of a financial liability. When calculating the effective interest rate, an entity shall estimate the expected cash flows by considering all the contractual terms of the financial instrument (for example, prepayment, extension, call, and similar options) but shall not consider the expected credit losses. The calculation includes all fees and points paid or received *unless it is immaterial or impracticable to determine reliably,* between parties to the contract that are an integral part of the effective interest rate (see paragraphs B5.4.1–B5.4.3), transaction costs, and all other premiums or discounts. There is a presumption that the cash flows and the expected life of a group of similar financial instruments can be estimated reliably. However, in those rare cases when it is not possible to reliably estimate the cash flows or the expected life	Until FY 2080/81

	financial instruments), the entity shall use the contractual cash flows over the full contractual term of the financial instrument (or group of financial instruments).	of a financial instrument (or group of financial instruments), the entity shall use the contractual cash flows over the full contractual term of the financial instrument (or group of financial instruments).	
Optional: The carve-out is optional. If an entity opts to use this carve-out that should be disclosed in the financial statements with its monitory impact in the financial statements as far as practicable.			
Para 5.5 Impairment	Recognition of expected credit losses General approach 5.5.1 **An entity shall recognise a loss allowance for *expected credit losses* on a financial asset that is measured in accordance with paragraphs 4.1.2 or 4.1.2A, a lease receivable, a *contract asset* or a loan commitment and a financial guarantee contract to which the impairment requirements apply in accordance with paragraphs 2.1(g), 4.2.1(c) or 4.2.1(d).** 5.5.2 An entity shall apply the impairment requirements for the recognition and measurement of a loss allowance for financial assets that are measured at fair value through other comprehensive income in accordance with paragraph 4.1.2A. However, the loss allowance shall be recognised in other comprehensive income and shall not reduce the carrying amount of the financial asset in the statement of financial position. 5.5.3 **Subject to paragraphs 5.5.13–5.5.16, at each reporting date, an entity shall measure the loss allowance for a financial instrument at an amount equal to the *lifetime expected credit losses* if the credit risk on that financial instrument has increased significantly since initial recognition.** 5.5.4 The objective of the impairment requirements is to recognise lifetime expected credit losses for all financial instruments for which there have been significant increases in credit risk since initial recognition — whether assessed on an individual or collective basis — considering all reasonable and supportable information, including that which is forward-looking. 5.5.5 **Subject to paragraphs 5.5.13–5.5.16, if, at the reporting**	**Impairment and uncollectibility of financial assets measured at amortised cost** (1) **An entity shall assess at the end of each reporting period whether there is any objective evidence that a financial asset or group of financial assets measured at amortised cost is impaired. If any such evidence exists, the entity shall apply paragraph 5 (given below) to determine the amount of any impairment loss** *unless the entity is a bank or financial institution registered as per Bank and Financial Institution Act 2073. Such entities shall measure impairment loss on loan and advances as the higher or amount derived as per the norms prescribed by Nepal Rastra Bank for loan loss provision and amount determined as per paragraph 5 (given below) and shall apply paragraph 5 (given below) to measure the impairment loss on financial assets other than loan and advances. The entity shall disclose the impairment loss as per this carve-out and amount of impairment loss determined as per paragraph 5 (given below).* (2) A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. It may not be possible to identify a single, discrete event that caused the impairment. Rather the combined effect of several events may have caused the impairment. Losses expected as a result of future events, no matter how likely, are not recognised. Objective evidence that a financial asset or group of assets is impaired includes observable data that comes to the attention of the holder of the asset about	Until FY 2080/81

date, the credit risk on a financial instrument has not increased significantly since initial recognition, an entity shall measure the loss allowance for that financial instrument at an amount equal to *12-month expected credit losses.*

5.5.6 For loan commitments and financial guarantee contracts, the date that the entity becomes a party to the irrevocable commitment shall be considered to be the date of initial recognition for the purposes of applying the impairment requirements.

5.5.7 If an entity has measured the loss allowance for a financial instrument at an amount equal to lifetime expected credit losses in the previous reporting period, but determines at the current reporting date that paragraph 5.5.3 is no longer met, the entity shall measure the loss allowance at an amount equal to 12-month expected credit losses at the current reporting date.

5.5.8 An entity shall recognise in profit or loss, as an *impairment gain or loss*, the amount of expected credit losses (or reversal) that is required to adjust the loss allowance at the reporting date to the amount that is required to be recognised in accordance with this Standard.

Determining significant increases in credit risk

5.5.9 At each reporting date, an entity shall assess whether the credit risk on a financial instrument has increased significantly since initial recognition. When making the assessment, an entity shall use the change in the risk of a default occurring over the expected life of the financial instrument instead of the change in the amount of expected credit losses. To make that assessment, an entity shall compare the risk of a default occurring on the financial instrument as at the reporting date with the risk of a default occurring on the financial instrument as at the date of initial recognition and consider reasonable and supportable information, that is available without undue cost or effort, that is indicative of significant increases in credit risk since initial recognition.

the following loss events:

(a) significant financial difficulty of the issuer or obligor;

(b) a breach of contract, such as a default or delinquency in interest or principal payments;

(c) the lender, for economic or legal reasons relating to the borrower's financial difficulty, granting to the borrower a concession that the lender would not otherwise consider;

(d) it becoming probable that the borrower will enter bankruptcy or other financial reorganisation;

(e) the disappearance of an active market for that financial asset because of financial difficulties; or

(f) observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group, including:

(i) adverse changes in the payment status of borrowers in the group (eg an increased number of delayed payments or an increased number of credit card borrowers who have reached their credit limit and are paying the minimum monthly amount); or

(ii) national or local economic conditions that correlate with defaults on the assets in the group (e.g. an increase in the unemployment rate in the geographical area of the borrowers, a decrease in property prices for mortgages in the relevant area, a decrease in oil prices for loan assets to oil producers, or adverse changes in industry conditions that affect the borrowers in the group).

5.5.10 An entity may assume that the credit risk on a financial instrument has not increased significantly since initial recognition if the financial instrument is determined to have low credit risk at the reporting date (see paragraphs B5.5.22–B5.5.24).

5.5.11 If reasonable and supportable forward-looking information is available without undue cost or effort, an entity cannot rely solely on *past due* information when determining whether credit risk has increased significantly since initial recognition. However, when information that is more forward-looking than past due status (either on an individual or a collective basis) is not available without undue cost or effort, an entity may use past due information to determine whether there have been significant increases in credit risk since initial recognition. Regardless of the way in which an entity assesses significant increases in credit risk, there is a rebuttable presumption that the credit risk on a financial asset has increased significantly since initial recognition when contractual payments are more than 30 days past due. An entity can rebut this presumption if the entity has reasonable and supportable information that is available without undue cost or effort, that demonstrates that the credit risk has not increased significantly since initial recognition even though the contractual payments are more than 30 days past due. When an entity determines that there have been significant increases in credit risk before contractual payments are more than 30 days past due, the rebuttable presumption does not apply.

Modified financial assets

5.5.12 If the contractual cash flows on a financial asset have been renegotiated or modified and the financial asset was not derecognised, an entity shall assess whether there has been a significant increase in the credit risk of the financial instrument in accordance with paragraph 5.5.3 by comparing:

(a) the risk of a default occurring at the reporting date (based on the modified contractual terms); and

(3) The disappearance of an active market because an entity's financial instruments are no longer publicly traded is not evidence of impairment. A downgrade of an entity's credit rating is not, of itself, evidence of impairment, although it may be evidence of impairment when considered with other available information. A decline in the fair value of a financial asset below its cost or amortised cost is not necessarily evidence of impairment (for example, a decline in the fair value of an investment in a debt instrument that results from an increase in the risk-free interest rate).

(4) In some cases the observable data required to estimate the amount of an impairment loss on a financial asset may be limited or no longer fully relevant to current circumstances. For example, this may be the case when a borrower is in financial difficulties and there are few available historical data relating to similar borrowers. In such cases, an entity uses its experienced judgement to estimate the amount of any impairment loss. Similarly, an entity uses its experienced judgement to adjust observable data for a group of financial assets to reflect current circumstances (see paragraph AG6 below). The use of reasonable estimates is an essential part of the preparation of financial statements and does not undermine their reliability.

(5) If there is objective evidence that an impairment loss on financial assets measured at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset shall be reduced either directly or through use of an allowance account. The amount of the loss shall be recognised in profit or loss.

(6) An entity first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant (see paragraph 2 above). If an entity determines that no objective

(b) the risk of a default occurring at initial recognition (based on the original, unmodified contractual terms).

Purchased or originated credit-impaired financial assets

5.5.13 Despite paragraphs 5.5.3 and 5.5.5, at the reporting date, an entity shall only recognise the cumulative changes in lifetime expected credit losses since initial recognition as a loss allowance for purchased or originated credit-impaired financial assets.

5.5.14 At each reporting date, an entity shall recognise in profit or loss the amount of the change in lifetime expected credit losses as an impairment gain or loss. An entity shall recognise favourable changes in lifetime expected credit losses as an impairment gain, even if the lifetime expected credit losses are less than the amount of expected credit losses that were included in the estimated cash flows on initial recognition.

Simplified approach for trade receivables, contract assets and lease receivables

5.5.15 Despite paragraphs 5.5.3 and 5.5.5, an entity shall always measure the loss allowance at an amount equal to lifetime expected credit losses for:

(a) trade receivables or contract assets that result from transactions that are within the scope of NFRS 15, and that:

(i) do not contain a significant financing component in accordance with NFRS 15 (or when the entity applies the practical expedient in accordance with paragraph 63 of NFRS 15); or

(ii) contain a significant financing component in accordance with NFRS 15, if the entity chooses as its accounting policy to measure the loss allowance at an amount equal to lifetime expected credit losses. That accounting policy shall be applied to all such

evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

(7) If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss shall be reversed either directly or by adjusting an allowance account. The reversal shall not result in a carrying amount of the financial asset that exceeds what the amortised cost would have been had the impairment not been recognised at the date the impairment is reversed. The amount of the reversal shall be recognised in profit or loss.

Application Guidance
(This guidance is an integral part of the above provisions)

AG1 Impairment of a financial asset measured at amortised cost is measured using the financial instrument's original effective interest rate because discounting at the current market rate of interest would, in effect, impose fair value measurement on financial assets that are otherwise measured at amortised cost. If the terms of a financial asset measured at amortised cost are renegotiated or otherwise modified because of financial difficulties of the borrower or issuer, impairment is measured using the original effective interest rate before the modification of terms. Cash flows relating to short-term receivables are not discounted if the effect of discounting is immaterial. If a financial asset measured at amortised cost has a variable interest rate, the discount rate for measuring any impairment loss under paragraph 5 (given above) is the current effective interest rate(s) determined under the contract. As a practical expedient, a creditor may measure impairment of a financial asset measured at amortised cost on the basis of an instrument's fair value using an observable market price. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash

	trade receivables or contract assets but may be applied separately to trade receivables and contract assets. (b) lease receivables that result from transactions that are within the scope of NFRS 16, if the entity chooses as its accounting policy to measure the loss allowance at an amount equal to lifetime expected credit losses. That accounting policy shall be applied to all lease receivables but may be applied separately to finance and operating lease receivables. 5.5.16 An entity may select its accounting policy for trade receivables, lease receivables and contract assets independently of each other. Measurement of expected credit losses **5.5.17 An entity shall measure expected credit losses of a financial instrument in a way that reflects:** **(a) an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes;** **(b) the time value of money; and** **(c) reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.** 5.5.18 When measuring expected credit losses, an entity need not necessarily identify every possible scenario. However, it shall consider the risk or probability that a credit loss occurs by reflecting the possibility that a credit loss occurs and the possibility that no credit loss occurs, even if the possibility of a credit loss occurring is very low. 5.5.19 The maximum period to consider when measuring expected credit losses is the maximum contractual period (including extension options) over which the entity is exposed to credit risk and not a longer period, even if that longer period is consistent with business practice.	flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable. **AG2** The process for estimating impairment considers all credit exposures, not only those of low credit quality. For example, if an entity uses an internal credit grading system it considers all credit grades, not only those reflecting a severe credit deterioration. **AG3** The process for estimating the amount of an impairment loss may result either in a single amount or in a range of possible amounts. In the latter case, the entity recognises an impairment loss equal to the best estimate within the range taking into account all relevant information available before the financial statements are issued about conditions existing at the end of the reporting period. **AG4** For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics that are indicative of the debtors' ability to pay all amounts due according to the contractual terms (for example, on the basis of a credit risk evaluation or grading process that considers asset type, industry, geographical location, collateral type, past-due status and other relevant factors). The characteristics chosen are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated. However, loss probabilities and other loss statistics differ at a group level between (a) assets that have been individually evaluated for impairment and found not to be impaired and (b) assets that have not been individually evaluated for impairment, with the result that a different amount of impairment may be required. If an entity does not have a group of assets with similar risk characteristics, it does not make the additional assessment. **AG5** Impairment losses recognised on a group basis represent an interim step pending the identification of impairment losses on individual assets in the group of financial assets that are collectively assessed for impairment. As soon as information is available that specifically identifies losses on	

	5.5.20 However, some financial instruments include both a loan and an undrawn commitment component and the entity's contractual ability to demand repayment and cancel the undrawn commitment does not limit the entity's exposure to credit losses to the contractual notice period. For such financial instruments, and only those financial instruments, the entity shall measure expected credit losses over the period that the entity is exposed to credit risk and expected credit losses would not be mitigated by credit risk management actions, even if that period extends beyond the maximum contractual period.	individually impaired assets in a group, those assets are removed from the group. **AG6** Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group. Entities that have no entity-specific loss experience or insufficient experience, use peer group experience for comparable groups of financial assets. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. Estimates of changes in future cash flows reflect and are directionally consistent with changes in related observable data from period to period (such as changes in unemployment rates, property prices, commodity prices, payment status or other factors that are indicative of incurred losses in the group and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience. **AG7** As an example of applying paragraph AG6, an entity may determine, on the basis of historical experience, that one of the main causes of default on credit card loans is the death of the borrower. The entity may observe that the death rate is unchanged from one year to the next. Nevertheless, some of the borrowers in the entity's group of credit card loans may have died in that year, indicating that an impairment loss has occurred on those loans, even if, at the year-end, the entity is not yet aware which specific borrowers have died. It would be appropriate for an impairment loss to be recognised for these 'incurred but not reported' losses. However, it would not be appropriate to recognise an impairment loss for deaths that are expected to occur in a future period, because the necessary loss event (the death of the borrower) has not yet occurred. **AG8** When using historical loss rates in estimating future cash flows, it is important that information about historical loss rates is applied to groups that are defined in a manner consistent with	

		the groups for which the historical loss rates were observed. Therefore, the method used should enable each group to be associated with information about past loss experience in groups of assets with similar credit risk characteristics and relevant observable data that reflect current conditions. **AG9** Formula-based approaches or statistical methods may be used to determine impairment losses in a group of financial assets (eg for smaller balance loans) as long as they are consistent with the requirements in paragraphs 5–7 and AG4–AG8. Any model used would incorporate the effect of the time value of money, consider the cash flows for all of the remaining life of an asset (not only the next year), consider the age of the loans within the portfolio and not give rise to an impairment loss on initial recognition of a financial asset.	

Non-Optional: The carve-out is not optional.

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